From Baird Equity Asset Management's
Mid Cap Growth Equity Investment Team:

Baird Equity Asset Management

Mid Cap Growth Equity 2nd Quarter 2016

Market Update

Economic activity rebounded from the sluggish first quarter of 2016, helping to support equities during much of the second calendar quarter. However, near term optimism quickly faded as the U.K. voted to leave the European Union late in June. The subsequent sharp selloff in stocks renewed fears of recession, political turmoil and isolationism. We expect global leaders, both political and central bankers, will continue offering fiscal and monetary support in order to avoid a broad economic slowdown or recession. In all likelihood, the economic ramifications of the vote will not be known for more than a year. Investors now have another set of variables to add to an already complicated market equation.

Portfolio Commentary

Clients of the Baird Mid Cap growth portfolios experienced results that modestly outpaced our primary benchmark, the Russell® Mid Cap Growth index, finishing the quarter in positive territory on an absolute basis. Gains early in the quarter were driven in part by a portfolio shift to a more pro-cyclical stance executed mid first quarter. Strong relative gains were realized in the consumer discretionary sector, while the healthcare, materials and technology sectors also contributed. Overall, we were pleased with the breadth of sectors contributing to performance. The financial services sector produced meaningful relative weakness as the post-Brexit impact of lower long term interest rates carried the day, particularly late in the quarter. Our sector thoughts and a more in depth description of portfolio changes follow.

The consumer discretionary sector led the way as several areas contributed even though performance from industry to industry varied widely. Specifically, Burlington Stores continued its impressive run as the off-price retail channel is one area capturing consumer dollars whereas many specialty retailers and apparel companies performed poorly. Dollar General also stood out as a strong performer on further fundamental strength, and we believe the outlook remains positive. Regarding portfolio changes, we sold Tiffany's as we believe the recent Brexit development further limits the potential for stronger global luxury spending. We also exited Under Armour following a confluence of building concerns, including heightened competition (with stalwart adidas seemingly getting its act together) and recent management changes. Proceeds were added to Burlington, Domino's Pizza and Tractor Supply. We also initiated a new position in Cable One, the 10th largest cable system operator in the U.S., which is primarily focused on secondary markets. In our view, Cable ONE's business is getting better as management focuses attention and capital on its faster growing, higher margin residential high speed data and business service segments.

The materials sector delivered solid relative performance. Little has changed in this part of the portfolio in recent quarters as the same stable of companies delivers solid fundamentals. Watsco, a distributor of HVAC equipment, and Acuity Brands, a commercial lighting solutions provider, have done the heavy lifting for some time. We believe these businesses remain well positioned to capture spending which is not robust in many parts of the world but is positive in commercial and residential construction markets.

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The technology sector added to relative performance based on strong returns from the software and services industry. This area has typically been the largest component of the portfolio's technology exposure as we tend to find more businesses with longer product cycles and higher recurring revenue than other areas within the sector. Notable performers included Tyler Technologies (IT services for local governments), Synopsys (electronic design automation for semiconductor chips) and Manhattan Associates (supply chain and logistics software solutions for retailers). Where we can find attractive growth and diversification, we will hold exposure to semiconductors, hardware or related businesses. Changes made during the quarter included the sale of semiconductor company Cavium, following a thesis changing and unexpected acquisition of a lower growth business. This deal announcement was an unfortunate turn of events soon after our purchase. We moved the capital into our other semiconductor holdings, Integrated Device Technology and Monolithic Power Systems. We also moved capital from Gartner to Akamai on what we view as better risk/reward potential. The portfolio remains in a slightly overweight position and despite the modest economic growth environment we believe the sector offers plenty of attractive opportunities.

Energy sector performance was a slight positive during the quarter. The sector return led the overall market due to a 25% advance in the price per barrel of oil. The overall performance impact was muted due to the sector's small absolute weight in both the benchmark and portfolio.

Healthcare was generally an area of favorable stock performance and portfolio holdings took the cue. Unlike recent years when sector strength was concentrated in Biotech and Specialty Pharma, returns were more balanced across the sector. We mentioned last quarter that we had done a fair amount of work on our structure in this sector adding two new positions, Edwards Lifesciences and Intuitive Surgical, and selling Envision Healthcare, Akorn and Perrigo. That work continued in the second quarter with the sale of Cerner, trim of Globus Medical, and purchase of Veeva Systems, a high growth, high margin software-as-a-service company focused on the healthcare industry. We view the company's newer product line as underappreciated by the market and expect it to drive substantial growth. Our belief is that the moves described above enhance the growth outlook and fundamental strength within the sector. The net of changes discussed above leave the portfolio slightly underweight the benchmark.

In the category of sounding like a broken record, if those even exist anymore, the consumer staples sector again delivered index-leading returns in the quarter. Our portfolio holdings outpaced benchmark performance with Dr. Pepper, McCormick and Church & Dwight leading the way. As far as changes, we sold Constellation Brands as this larger market cap name exited the benchmark. While we think the outlook for Constellation is quite positive, it has been our discipline to exit names that stretch the upper end of market cap when they leave the Russell® Mid Cap Growth Index. To offset the Constellation sale, late in the quarter we initiated a position in Casey's General Stores, an operator of convenience stores and gasoline stations primarily located in Midwestern states. The convenience store industry is large and fragmented, and we believe Casey's is well-position in its smaller markets to sustain attractive long-term earnings growth. The leadership of the consumer staples sector in recent years strikes us as unusual in an upward trending market given the slower top-line growth characteristics of many of the companies. However, investors have clearly been drawn to the relatively stable nature of the staples businesses, the opportunity to earn reasonable dividend yields and the lure of merger premiums as consolidation has found its way to the sector. This combination, particularly in our low interest rate world, has driven stock prices and valuations higher throughout the sector. We are mindful of all these factors as we structure portfolio holdings in this area.

The producer durables sector ended on the positive side of the ledger, but modestly. Returns were more muted than the first quarter as the wait for a meaningful turn in manufacturing activity continued. We shifted the sector's mix a bit during the first quarter, positioning for stable to improving activity in the industrial economy. As a result the portfolio carried an overweight position into the second quarter versus equal weight at year end. Changes in the second quarter were relatively modest with additions to Graco (leader in industrial fluid handling equipment) and Rockwell (manufacturing automation) by way of trims to Stericycle (medical waste disposal) and Genpact (IT process outsourcing).

Financials drove the largest relative underperformance as the combination of a disappointing jobs report in early June and market volatility surrounding the Brexit vote pressured long term interest rates. Performance headwinds were felt broadly in the sector with notable weakness from Affiliated Managers, Euronet, and Alliance Data. Our financial structure has remained relatively constant in recent quarters with some adds and trims based on market movement. During periods when the growth outlook has been stable to improving, the portfolio's structure has performed as expected. The difference in the second quarter and particularly the last few weeks of June was the sharp sell-off across market and credit sensitive names amid the drop to all-time lows for the U.S. 10-year Treasury. Not unexpectedly in this environment, REITs (no portfolio exposure) compounded the challenge by advancing sharply. We have conviction in the quality of our financial names but will continue to assess our sector structure.

Outlook

Looking to the back half of the year, we are mindful of the current expansion's duration, noise surrounding our national elections in November and the potential negative repercussions from Brexit on global growth. We anticipate some moderation in second-half earnings forecasts from managements, but expect that U.S. economic fundamentals are strong enough to support continued growth.

The silver lining for mid cap clients rests on the nature of the companies in which we invest. Many of the businesses are entirely or mostly domestic, insulating them to some degree from international events and associated currency swings. The companies' relatively smaller size also helps as their sustainable growth rates are higher than many of their larger, more global counterparts. Finally, well-managed businesses with strong balance sheets and cash generation possess the flexibility to make sound long term decisions for shareholders, such as business reinvestment, repurchasing stock or making strategic acquisitions. As mentioned in the opening paragraph, the many inputs working into the market equation make for a challenging investment environment. The unexpected result from the U.K. referendum and ensuing volatility is just one more example. As in the past, we will work to use market dislocation to improve the quality and growth rate of our portfolios. On behalf of everyone at Baird Equity Asset Management, we thank you for your support of our Mid Cap Growth strategy.

Top 5 Portfolio Contributors			Bottom 5 Portfolio Contributors		
Security	**Avg. Weight**	**Contribution**	**Security**	**Avg. Weight**	**Contribution**
Tyler Technologies (TYL)	1.91	0.50	WABCO Holdings (WBC)	1.87	-0.28
A.O. Smith (AOS)	2.68	0.41	Harman International (HAR)	1.24	-0.32
Burlington Stores (BURL)	2.23	0.39	Stericycle (SRCL)	1.50	-0.33
IDEXX Laboratories (IDXX)	1.96	0.34	Affiliated Managers Group (AMG)	2.47	-0.33
Acuity Brands (AYI)	2.57	0.33	Cavium (CAVM)	0.76	-0.40

The Baird Equity Asset Management Mid Cap Growth Equity commentary is incomplete if not accompanied with the most recent performance report.

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Tenured Mid Cap Growth Investment Team

- All investment team members have equity ownership
- Deep sector expertise
- Average years of experience: 19 years

Investment Professional	Years of Experience	Years with Baird	Coverage Responsibility	Educational Background
Chuck Severson, CFA *Senior Portfolio Manager and Analyst*	29	29	Industrials & Materials	MS – Finance - The Applied Security Analysis Program BBA – Accounting and Finance (UW – Madison)
Ken Hemauer, CFA *Senior Portfolio Manager and Analyst*	22	22	Financial Services Consumer Discretionary	MS – Finance - The Applied Security Analysis Program BBA – Finance (UW – Madison)
Doug Guffy *Senior Research Analyst*	32	12	Energy & Industrials	MBA – Finance (Ball State University) BA – Economics & Government (Anderson University)
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